COMPTROLLER OF THE CURRENCY
BANK ACCOUNTING ADVISORY SERIES
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This edition of the Bank Accounting Advisory Series (BAAS) expresses the Office of the Chief Accountant's current views on accounting topics of interest to national banks. Banks prepare their Consolidated Reports of Condition and Income (call reports) using generally accepted accounting principles (GAAP) and regulatory requirements. Accordingly, responses contained in the series are based on GAAP and regulatory requirements.

These advisories are not official rules or regulations of the Comptroller of the Currency (OCC). Rather, they represent either interpretations by the OCC's Office of the Chief Accountant of generally accepted accounting principles, or OCC interpretations of regulatory capital requirements.

Nevertheless, national banks that deviate from these stated interpretations may be required to justify those departures to the OCC. The series is intended to inform the banking community of the Office's views and rationale on issues of broad accounting interest. Additional releases will be issued in the future on emerging accounting issues that affect banks.

In June 2009, the Financial Accounting Standards Board (FASB) issued Statement No. 168, The FASB Accounting Standards Codification TM and the Hierarchy of Generally Accepted Accounting Principles (FAS 168), to establish the FASB Codification as the single source of authoritative nongovernmental U.S. GAAP. All guidance contained in the FASB Codification carries an equal level of authority and all previously existing accounting standards (such as FASB Statements, Emerging Issues Task Force Issues, and Accounting Principles Board Opinions) have been superseded as described in FAS 168. The FASB Codification became effective for all interim and annual periods after September 15, 2009 (effectively as of September 30, 2009). References within the Bank Accounting Advisory Series to specific pre-Codification standards under U.S. GAAP should be understood to mean the corresponding reference in the FASB's Accounting Standards Codification.

A number of accounting rules have changed since the last publication of the Bank Accounting Advisory Series and as such, many sections of this document have been significantly updated and modified. The following sections have been revised in their entirety in this edition.

1B: Other-Than-Temporary Impairment
9A: Accounting for Transfers of Financial Assets and Securitizations
10A: Accounting for Acquisitions
11D: Fair Value Accounting

2C. COMMITMENTS

Facts:

A bank has off-balance sheet financial instruments, such as commitments to extend credit, guarantees, and standby letters of credit that are subject to credit risk. These financial instruments are off-balance sheet in accordance with GAAP and are not considered to be derivatives under Statement of Financial Accounting Standards No. 133 (SFAS 133). The bank evaluates and estimates the credit losses associated with these off-balance sheet instruments. In some instances the counterparty to the off-balance sheet instrument is also a borrower of the bank.

Question 1: (September 2004)

Should the bank record a provision for credit losses on off-balance sheet financial instruments, such as standby letters of credit, to the ALLL or to a separate liability account?

Staff Response:

In accordance with the American Institute of Certified Public Accountant's (AICPA) Audit and Accounting Guide for Depository and Lending Institutions: Banks and Savings Institutions, Credit Unions, Finance Companies and Mortgage Companies and the call report instructions, credit losses related to off-balance sheet financial instruments, such as standby letters of credit, should be accrued and reported separately as liabilities and not reported in the allowance for loan and lease losses (ALLL). This is the appropriate treatment even if the counterparty of the off-balance sheet financial instrument is also a borrower of the bank. However, GAAP stipulates that the recognition of the provision for losses must meet the criteria set forth in the Statement of Financial Accounting Standards No. 5 (SFAS 5), which requires recognition of a loss if the loss is both probable and the amount reasonably estimable. The AICPA's guidance also notes that the methodology used for evaluating "loan losses" may be useful in evaluating and estimating credit losses for these off-balance sheet financial instruments.

Question 2: (February 2004)

Can the bank include the liability for off-balance sheet credit exposure in Tier 2 capital for risk-based capital purposes?

Staff Response:

Yes. Previously, the ALLL included a component for credit exposure related to off-balance sheet instruments. Accordingly, the risk-based capital requirements have been revised so that banks may continue to include this liability for off-balance sheet credit